

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
LIQUOR DEPOT, INC.	:	
for Revision of a Determination or for Refund of Sales	:	
and Use Taxes under Articles 28 and 29 of the Tax	:	
Law for the Period December 1, 1991 through	:	
February 29, 1996.	:	

In the Matter of the Petition	:	DETERMINATION
of	:	DTA NOS. 817501
FRANK ACETO	:	AND 817502
for Revision of a Determination or for Refund of Sales	:	
and Use Taxes under Articles 28 and 29 of the Tax	:	
Law for the Period December 1, 1993 through	:	
February 29, 1996.	:	

Petitioner Liquor Depot, Inc., 3258 Hempstead Turnpike, Levittown, New York 11756, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1991 through February 29, 1996.

Petitioner Frank Aceto, 16 West 3rd Street, Freeport, New York 11520-5729, filed a petition for revision of a determination or for refund of sales and use taxes under Articles 28 and 29 of the Tax Law for the period December 1, 1993 through February 29, 1996.

A consolidated hearing was held before Winifred M. Maloney, Administrative Law Judge, at the offices of the Division of Tax Appeals, 641 Lexington Avenue, New York, New York on

December 6, 2000 at 11:00 A.M. and continued to completion at the same location on February 20, 2001, with all briefs to be submitted by September 7, 2001, which date began the six-month period for the issuance of this determination. Petitioners appeared by Kestenbaum & Mark (Bernard S. Mark, Esq., of counsel). The Division of Taxation appeared by Barbara G. Billet, Esq. (Nicholas A. Behuniak, Esq., of counsel).

ISSUES

- I. Whether Liquor Depot properly reported its taxable sales during the period in issue.
- II. Whether petitioners have shown reasonable cause for abatement of penalties.

FINDINGS OF FACT

1. Petitioner Frank Aceto is the president and sole shareholder of petitioner Liquor Depot, Inc. ("Liquor Depot"). Liquor Depot, doing business as Buy Rite Liquor Depot, a retail liquor store, began operations in April 1991 in Levittown, New York at a location which was a vacant former liquor store. The liquor store, containing 1,000 square feet of selling space, is in a strip shopping center located in a middle class suburban area of Long Island, Nassau County. During the period in issue, Liquor Depot's hours of operation were Monday through Wednesday, 9:00 A.M. through 8:00 P.M., and Thursday through Saturday, 9:00 A.M. through 9:00 P.M.

2. On May 26, 1998, the Division of Taxation (the "Division") issued to Liquor Depot a Notice of Determination for sales and use taxes due for the period December 1, 1991 through February 29, 1996 asserting tax due in the amount of \$158,458.58, interest due of \$109,971.32 and penalty due of \$65,603.51, for a total due of \$334,033.41.

On the same date, the Division issued to Frank Aceto, a Notice of Determination for sales and use taxes due for the period December 1, 1993 through February 29, 1996 asserting tax due in the amount of \$81,091.22, interest due of \$39,414.84 and penalty due of \$33,109.26, for a

total due of \$153,615.32. The notice was issued to Frank Aceto as an officer or person responsible for the taxes due from Liquor Depot.

3. At the hearing, petitioners stipulated that Mr. Aceto is a responsible officer for any additional sales taxes found to be due for the period December 1, 1993 through February 29, 1996.

4. On December 12, 1994, the Division assigned Brian McCann, Tax Auditor I, to conduct a field audit of Liquor Depot. Mr. McCann has been employed by the Division for approximately 22 years. Prior to the audit in this matter, he had conducted approximately six audits of retail liquor stores. An additional Division employee, the auditor's supervisor, Mr. William Welthy, Tax Auditor II, was also involved in this audit. Mr. Welthy has supervised 50 audits of retail liquor stores.

5. The audit originated because of discrepancies in information contained in Liquor Depot's sales tax returns and information received by the Division's Research and Discovery Bureau from Liquor Depot's wholesale liquor suppliers concerning its purchases of merchandise.

6. The auditor issued an audit appointment letter and request for books and records dated January 13, 1995, which provided that: "all books and records pertaining to your sales and use tax liability for the period [12/01/91 through 11/30/94] are to be available on the [to be scheduled] appointment date. This would include journals, ledgers, sales invoices, purchase invoices, cash register tapes, federal income tax returns, and exemption certificates." This letter, which was accompanied by, among other things, an attached checklist again specifying the records required for audit, also noted that additional information might be required during the course of the audit.

7. On May 26, 1995, the auditor mailed third-party verification forms to various wholesale liquor suppliers requesting information concerning the amount of purchases made by Liquor Depot during the period December 1, 1991 through November 30, 1994. Subsequently, in July 1995, the auditor sent out second requests for third-party information on Liquor Depot's purchases.

8. The first field audit appointment took place on June 27, 1995 at the liquor store. Present during that appointment were the auditor, his supervisor, Mr. Aceto and his accountant, Burt Kroll. At that initial appointment, Liquor Depot's business operations and record keeping were discussed and some records were supplied for the auditor's review.

The auditor was not supplied with either Liquor Depot's cash register tapes or sales journals. Liquor Depot did not maintain either a sales journal or a cash receipts journal. Cash register tapes were not maintained and were not used in record keeping. Mr. Kroll prepared the sales tax returns by computing the sales based on deposits listed on the bank statements. A purchase journal was not provided to the auditor. Liquor Depot would receive an invoice for each order it placed with its suppliers. However, the purchase invoices from Liquor Depot's suppliers were not provided to the auditor. Liquor Depot paid for some of its liquor and wine purchases by check. However, for many of its liquor and wine purchases, Liquor Depot paid cash directly to its liquor suppliers' salespeople who usually stopped in once a week. No receipts reflecting those payments of cash to the suppliers' salespeople were provided to the auditor. The books and records provided to the auditor consisted of Liquor Depot's federal income tax returns for the years 1991, 1992, 1993 and 1994, bank statements for the period December 1991 through December 1994, the check disbursements journal and canceled checks for the period December 1993 through November 1994.

9. The auditor received written purchase verifications from nine wholesale liquor suppliers, seven of which confirmed significant purchases by Liquor Depot for the period December 1991 through November 1994. The most substantial purchases were confirmed by Peerless Importers, Inc. ("Peerless") and Star Industries, Inc. ("Star"). The auditor observed that according to the figures provided by the liquor suppliers, Liquor Depot's purchases substantially exceeded sales reported on its sales tax returns for the period December 1, 1991 through November 30, 1994. Based on the purchase information received from the nine suppliers, the auditor calculated Liquor Depot's purchases to be \$1,320,763.77 for the period December 1991 through November 1994. Gross sales in the total amount of \$392,786.00 were reported on Liquor Depot's sales tax returns for the period December 1, 1991 through November 30, 1994.

10. Utilizing information from Liquor Depot's federal corporate income tax returns (sales minus sales tax included, divided by cost of goods sold), the auditor calculated Liquor Depot's markup to be 36.05%, 78.34%, 71.06% and 104.65%, for the years 1991, 1992, 1993 and 1994, respectively. Based on his prior audit experience and knowledge of liquor industry norms with respect to the markup on sales, the auditor decided it was necessary to ask Mr. Aceto what Liquor Depot's actual markup was.

11. On February 1, 1996, a second field audit appointment took place at the liquor store. In attendance were the auditor, his supervisor and Messrs. Aceto and Kroll. The audit findings to date and Liquor Depot's markup on liquor and wine were among the things discussed at that appointment. The auditor was unable to perform an actual markup test during that appointment because no current purchase invoices were at the store. Copies of the audit work papers were supplied to Mr. Aceto at that time.

12. As the audit continued, the period under review was updated to cover the period December 1, 1991 through February 29, 1996. On April 8, 1996, the auditor sent third-party verification forms to Liquor Depot's major suppliers for the period December 1, 1994 through February 29, 1996. In May 1996, second requests were sent to some of the suppliers. The auditor received responses from seven suppliers, including Star. The auditor observed that, for the period December 1, 1994 through February 29, 1996, the figures provided by Liquor Depot's major suppliers substantially exceeded sales reported on its sales tax returns. For the period December 1994 through February 1996, a total of \$673,126.43 in purchases by Liquor Depot was confirmed by the seven suppliers. For the period December 1, 1994 through February 29, 1996, a total of \$278,441.00 in gross sales was reported on Liquor Depot's sales tax returns.

13. The record includes the two responses received by the auditor from the supplier Star. The first handwritten confirmation covered the period January 1992 through December 1994 inclusive. Star confirmed purchases by Liquor Depot in each month of that period totalling \$494,073.00. The second handwritten confirmation covered the period December 1994 through February 1996 inclusive. Star confirmed purchases by Liquor Depot in each month of that period totalling \$94,900.00. In each of the confirmations, Star reported \$22,375.00 in purchases by Liquor Depot for the month of December 1994. The two separate handwritten confirmations were signed by two different Star credit department employees. For the period January 1992 through February 1996 inclusive, Star confirmed a total of \$566,598.00 in purchases by Liquor Depot.

14. On August 1, 1996 and December 30, 1996, the auditor spoke with Mr. Aceto by telephone about the audit's progress to date, including the updating of the audit period to cover

the period December 1, 1991 through February 29, 1996. During the latter telephone conversation, a third field audit appointment was tentatively scheduled for January 21, 1997.

The third field audit appointment took place on January 23, 1997 at the liquor store with the auditor, his supervisor, Mr. Kroll and Mr. Aceto in attendance. At that appointment, the audit findings to date, including the expansion of the audit period to cover the period December 1, 1991 through February 29, 1996, were reviewed. At that time, the auditor also orally requested all Liquor Depot's books and records pertaining to its sales tax liability for the expanded audit period.

15. The auditor mailed a letter to Mr. Aceto, dated January 23, 1997, which confirmed previous discussions concerning the updating of the audit period to cover the period December 1, 1991 through February 29, 1996. The letter requested that Mr. Aceto provide Liquor Depot's books and records pertaining to the sales tax liability for the period under audit including "journals, ledgers, sales invoices, purchase invoices, cash register tapes, federal income tax returns and exemption certificates." The letter included, among other things, a checklist of records to be provided to the auditor for review. The federal income tax return for the year 1996 was specifically requested on the checklist.

16. On January 30, 1997, Mr. Aceto called the auditor to discuss, among other things, his disagreement with the third-party purchase information provided by the supplier Star. During that telephone conversation, Mr. Aceto informed the auditor that he was trying to get information together and requested a copy of the third-party information from Star. On the same date, the auditor sent Mr. Aceto the requested information.

17. The fourth and final field audit appointment took place at the liquor store on August 7, 1997. At that appointment, the auditor, with his supervisor in attendance, went over the audit

findings and status of the case with Messrs. Aceto and Kroll. Mr. Aceto objected to the amount of purchases from the various liquor and wine suppliers that the auditor determined had been made by Liquor Depot, especially its purchases from the supplier Star. Mr. Aceto claimed that Liquor Depot's purchases from Star were nominal, totaling only \$6,391.03, for the period in issue. The auditor instructed Mr. Aceto to go back to the suppliers and remedy any alleged problems with such suppliers. He also instructed Mr. Aceto to ask the suppliers for signed delivery ticket information and, if possible, to have the suppliers send any information directly to the auditor. Mr. Aceto reiterated that his basic markup on liquor was 20% and on wine was 40%. He also informed the auditor that he had sales over the years and accepted competitor's coupons.

At that appointment, for the first time, Mr. Aceto claimed that he had made substantial nontaxable sales to exempt organizations. He also claimed that he was charging approximately 3% over cost to exempt organizations on their purchases. Mr. Aceto provided a looseleaf binder containing information and summary sales ledger sheets that he claimed supported nontaxable sales of approximately \$1,041,907.50 to exempt organizations for the period December 1, 1991 through December 31, 1995. He allowed the auditor to take the looseleaf binder and summary sales ledger sheets back to his office, where the auditor transcribed the information. Subsequently, the looseleaf binder and the summary sales ledger sheets were returned to Mr. Aceto.

18. During the period in issue, gross sales reported and taxable sales reported on the sales tax returns were the same. No sales exempt from taxation were reported on the sales tax returns. For the period December 1, 1991 through February 29, 1996, a total of \$671,227.00 in gross and taxable sales was reported.

Liquor Depot never disclosed any of the sales it claimed were tax exempt on any of its federal or state tax returns even though the respective returns require such disclosure.

19. The looseleaf binder provided to the auditor contained exemption certificates and sheets of looseleaf paper. Each certificate was followed by one or more sheets of looseleaf lined paper on which handwritten dates and dollar amounts appeared in pencil. No itemized sales invoices for any of the claimed sales to the various organizations were included in the binder. A review of the certificates by the auditor revealed that the vendor portion was not filled in on the majority of the certificates and most of the dates written on the certificates were prior to the date on which Liquor Depot began business. Addresses listed for some of the organizations were incomplete. Summary sales ledger sheets for claimed sales to alleged exempt organizations during 1995 were presented to the auditor as well. Listed on those summary sales ledger sheets were daily individual sale amounts and total amounts that represented total daily dollar sales that Liquor Depot claimed were made to alleged exempt organizations each day. The summary sales ledger sheets also had a summary total for each month and the total for the year. The summary sales ledger sheets did not provide any information about which organization made the purchase, the exact products sold and the price at which they were sold. Given the magnitude of claimed nontaxable sales, the auditor decided to confirm the amount of Liquor Depot's claimed exempt sales directly with each organization listed on the certificates.

20. The auditor sent written purchase confirmation requests to 23 organizations to which Liquor Depot claimed it made nontaxable sales, using the addresses listed on their respective exempt certificates. Whenever the auditor learned of a better address for an organization, he sent a written confirmation request to that organization at the corrected address. Even though the auditor attempted to get the correct addresses for all of the organizations to which Liquor Depot

claimed it made tax exempt sales, six organizations never responded to the Division's written requests for confirmation and five confirmation requests were returned by the United States Postal Service ("USPS") as undeliverable. One of the undeliverable confirmation requests was addressed to the Swiss Benevolent Society.

Twelve of the tax exempt entities to which Liquor Depot claimed it made sales responded to the Division's written requests for confirmation. Of the twelve, only two tax exempt entities, the Disabled American Veterans of Nassau County and the Levittown Kiwanis, confirmed a total of \$776.16 in purchases from Liquor Depot between December 1991 and February 1996. Of the 12 tax exempt entities that responded, Liquor Depot claimed it made approximately \$313,763.36 in sales to such entities. Three of the entities that petitioners claimed were tax exempt turned out, in fact, not to be tax exempt.

21. On August 19, 1997, the auditor sent Mr. Aceto a letter requesting Liquor Depot's previously unprovided books and records including, among other items, its federal income tax returns for the years 1995 and 1996. The letter also gave Mr. Aceto the option of having a physical markup test performed at the store.

22. On August 29, 1997, the auditor received a letter, dated August 28, 1997, from Phyllis Valenti, Star's controller. In that letter, Ms. Valenti stated, in pertinent part, as follows:

Yesterday, on August 27, one of our former accounts named Liquor Depot came down to see Star, in reference to the [previously confirmed] sales figures, that were given to you by Star. Looking at them I noticed that on one [confirmation] sheet the year 1994 only has a sale figure in their [sic] for the month of Dec. 94, while the other [confirmation] sheet has the whole year of 1994 filled in. I also noticed that they were done by different people, and different times. We are out of the wholesale distribution business since Aug. 1, 1996 and our main frame computer we no longer have, I can not [sic] go back and see if these figures are accurate.

I can tell you that I have been working for Star for over 20 years, I am the controller here, and in my experience I do not feel these figures that were given to

you are accurate, and from other times they have given the wrong figures for a different customer. Being I can not [sic] check this out, I must conclude these figures are wrong. . . .

23. As the audit progressed into the fall of 1997, the auditor called Mr. Aceto and reminded him that various pieces of previously requested information had not been supplied. On January 29, 1998, Mr. Aceto and the auditor had a telephone conversation concerning, among other things, his disagreement with the purchase information supplied to the auditor by Liquor Depot's suppliers, especially Star. Mr. Aceto specifically asked the auditor about the August 28, 1997 letter from Star. The auditor informed Mr. Aceto that he did not find the letter to be credible because it contained erroneous information and also did not contain any revised figures, with backup. The auditor further informed Mr. Aceto that the information originally supplied to the auditor by the suppliers would be used unless proper documentation could be supplied to refute that information. Mr. Aceto assured the auditor that he would go to Star's offices within the next few days to see what documentation he could get.

24. Mr. Aceto never supplied any additional books and records for the period December 1991 through February 1996. No further information was received from any of Liquor Depot's suppliers.

25. The auditor's review of the books and records provided by Liquor Depot indicated that those records were inadequate to determine sales for the audit period. The auditor determined that in order to calculate Liquor Depot's sales it was first necessary to confirm Liquor Depot's purchases from its various liquor and wine suppliers. The auditor sent out requests to Liquor Depot's suppliers to confirm the amount of purchases made by it during the period December 1991 through November 1994. As the audit period was extended, the auditor sent out third-party purchase confirmation requests to Liquor Depot's major suppliers for the

period December 1994 through February 1996. For the period December 1, 1991 through February 29, 1996, the auditor confirmed a total of \$1,993,890.20 in purchases by Liquor Depot from its major suppliers.

26. The auditor's review of canceled checks for the 12-month period December 1993 through November 1994 revealed additional purchases in the amount of \$5,136.50 from small suppliers that had not been confirmed by the third-party verification. Using that information, the auditor estimated that Liquor Depot purchased approximately \$428.04 ($\$5,136.50 \div 12$) from unconfirmed small suppliers each month. The auditor projected that estimated monthly amount over the audit period and calculated a total of \$21,830.06 in purchases by Liquor Depot from small suppliers during the period December 1, 1991 through February 29, 1996.¹

27. The auditor calculated Liquor Depot's total audited purchases for the period December 1, 1991 through February 29, 1996 to be \$2,015,720.26, by adding the total estimated purchases from small suppliers to the total purchases confirmed by major suppliers (\$21,830.06 + \$1,993,890.20).

28. The auditor computed an inventory adjustment of \$44,155.00 by subtracting \$14,850.00, the closing inventory on December 31, 1994 as reported on the 1994 federal corporate income tax return, from \$59,005.00, the inventory on December 31, 1991 as reported on the 1991 federal corporate income tax return.² The auditor added the inventory adjustment of \$44,155.00 to total audited purchases and computed total purchases available for sale to be \$2,059,875.26.

¹ (24 months [Dec. 1991 - Nov. 1993] x \$428.04 per month) + \$5,136.50 (Dec. 1993 - Nov. 1994) + (15 months [Dec. 1994 - Feb. 1996] x \$428.04 per month) = \$21,830.06

² The auditor was supplied with Liquor Depot's federal income tax returns for the years 1991 through 1994 only.

29. The auditor calculated a 1½% (\$30,898.14) pilferage and breakage allowance based upon the Audit Division's experience in the liquor retail industry and because the adjustment is required by Field Audit Management. The auditor subtracted the \$30,898.14 pilferage allowance from the total purchases available for sale. This resulted in cost of goods sold of \$2,028,977.12.

30. The auditor then applied a markup percentage to the cost of goods sold to arrive at the audited sales. On more than one occasion during the audit, Mr. Aceto explained that Liquor Depot's markup was 20% on liquor and 40% on wine. During one field appointment, the auditor performed a limited markup test of Liquor Depot's products, using one current invoice, and the results of the test confirmed a markup of 20% on liquor and 40% on wine. Mr. Aceto declined to have a much more detailed markup test performed on the store inventory. He also explained that Liquor Depot's sales were evenly split between liquor and wine. In order to be conservative, the auditor calculated the markup percentage on a sales mix of 60% liquor and 40% wine. The auditor calculated the markup percentage to be 28%.³ Then, the auditor reduced the markup percentage by 3% to 25% to account for special sales, and any significant discounts offered by Liquor Depot to its customers.

31. The auditor then applied the markup percentage of 25% to Liquor Depot's cost of goods sold of \$2,028,977.12 to arrive at audited sales of \$2,536,221.45. The auditor subtracted \$776.16 in verified exempt sales (Finding of Fact "20") from the audited sales to arrive at audited taxable sales of \$2,535,445.29. Subtracting the taxable sales reported by Liquor Depot on its sales tax returns for the audit period of \$671,227.00, the auditor determined additional

³ Liquor .60 x 20 % = .12
Wine .40 x 40 % = .16
 .28 overall markup

taxable sales for the audit period of \$1,864,218.29. Applying the tax rate of 8.25% resulted in \$158,458.58 in tax due.

32. Penalties were asserted for failure to pay the tax due. An additional penalty was imposed as a result of the underreporting of tax due exceeding 25% of the amount of the taxes required to be shown on the returns for the audit period.

33. On May 8, 1998, the Division issued a Statement of Proposed Audit Adjustment to Liquor Depot setting forth tax due of \$158,458.58, interest of \$108,387.75 and penalty of \$63,383.42, for a total due as of that date of \$330,229.75.

34. Between February 27, 1995 and November 5, 1997, Liquor Depot, by Mr. Aceto, as president, executed five consents extending the period of limitation for assessment of sales and use taxes due under articles 28 and 29 of the Tax Law for the period December 1, 1991 through May 31, 1995 to June 20, 1998.

35. During the audit, Mr. Aceto, as officer of Liquor Depot, executed two consents extending the period of limitation for assessment of sales and use taxes under articles 28 and 29 of the Tax Law which collectively extended to June 20, 1998 the date by which the Division could assess tax due for the period December 1, 1993 through May 31, 1995.

36. As noted in Finding of Fact "2", the Division issued a Notice of Determination, dated May 26, 1998, to petitioner Liquor Depot and a Notice of Determination, dated May 26, 1998, to petitioner Frank Aceto.

37. For approximately five or six years prior to opening Liquor Depot, Mr. Aceto owned and operated a liquor store that had gone out of business. Prior to owning that earlier liquor store, Mr. Aceto worked as a manager in the bar business for a number of years. Mr. Aceto attended two years of college where he majored in business administration.

38. Mr. Aceto negotiated the terms of the lease with the landlord. During the audit period, the rent for the store was approximately \$4,100.00 per month. He also negotiated a home equity loan, the proceeds of which were used to supply the funds needed to purchase the inventory to stock Liquor Depot. Mr. Aceto negotiated the purchase arrangements with the wholesale liquor suppliers. He also resolved any payment issues concerning Liquor Depot's purchases with the liquor suppliers' credit managers. Within a few months of opening, Liquor Depot began paying many of its suppliers in cash.

39. Liquor Depot placed orders for merchandise with various liquor and wine suppliers. When Liquor Depot received the merchandise it ordered, it would also receive a purchase order. Any broken bottles and short shipped or back ordered items were noted on the purchase invoice by the supplier's driver who delivered the merchandise. In order to return a spoiled bottle of wine or liquor or an incorrectly ordered item, Liquor Depot was required to call the supplier and have the item picked up. Special memos were issued to Liquor Depot for each item picked up by the suppliers. Mr. Aceto maintained the purchase invoices and the memos to determine the amount due the suppliers for the merchandise delivered. On occasion, there would be a discrepancy between the amount appearing due on a supplier's monthly statement and the amount that Mr. Aceto had paid. Mr. Aceto used the purchase invoices and the memos to resolve the discrepancies.

40. Petitioners submitted into evidence purchase summary sheets prepared by Mr. Aceto which purport to be a summary of all original purchase invoices substantiating Liquor Depot's purchases from five of its suppliers, including Peerless and Star, for the audit period. Each supplier's purchase summary sheets list in columnar form, on a monthly basis, the invoice amounts, the amounts determined by the auditor through the third-party verification and the

difference between the two amounts. Mr. Aceto also prepared a summary schedule on which the total purchases made from each of the five suppliers are listed for the entire audit period. On the summary schedule, for each of the five suppliers, the amount listed as the purchase invoices total for the entire audit period is less than the amount listed as the third-party verification total determined by the auditor. For the supplier Star, the purchase invoices total for the audit period is listed as \$6,391.03 and the third-party verification total for the audit period is listed as \$566,598.00, a difference of \$560,206.97.

41. Although petitioners claim to have available a box full of purchase invoices that would substantiate all of the figures provided on the purchase summary sheets, only the actual purchase invoices that represented Liquor Depot's purchases from the supplier Peerless during 1995 were submitted into evidence.

42. The Division supplied a questionnaire to Ms. Phyllis Valenti, the author of the August 28, 1997 letter. Ms. Valenti responded in writing on December 1, 2000. The Division submitted her response into the record. Ms. Valenti was the controller of Star for the years 1994 through 1997. As controller, she was responsible for, among other things, the computer department, the credit department, the order board, accounts receivable and customer service. During 1992 through 1996, Star maintained a record keeping system for its sales to liquor stores. At 1:00 P.M., orders that were placed by liquor stores in the morning were billed up every hour on the hour until 5:00 P.M. The invoices were given to the warehouse for routing and in the morning the drivers were given the run for the day. After a delivery was made, the signed invoice came back and a copy was filed by invoice number, with each month's invoices kept together. A sales report was generated by the computer on a daily basis. Sales were recorded daily on a spread sheet and then posted to the general ledger monthly. Ms. Valenti was not involved in the billing

process for the years 1992 through 1996. Rather, the credit managers maintained records for each purchaser and it was the credit manager who was responsible for supervising preparation of the written confirmations requested by the Division. Written confirmations were prepared using computer-generated sales reports. During her years as controller, Ms. Valenti found that Star had sent inaccurate information to the Division numerous times. Usually the inaccurate information resulted because the Star employee assigned to prepare the written confirmation obtained the sales information from the wrong account. She could not recall the basis for the opinion set forth in her August 28, 1997 letter to the auditor that the information provided to the auditor regarding Liquor Depot might be inaccurate.

43. In an effort to further clarify Ms. Valenti's December 1, 2000 responses as well as her August 28, 1997 letter, the Division sent Star a written questionnaire and requested that it be completed. Star did not complete the questionnaire. Rather, its response consisted of the affidavit of Phyllis Valenti, assistant vice president of Star.

44. Prior to July 1996, Star was in the wholesale wine and liquor distribution business. Since that date Star has been in the wine and liquor import business. Upon entering the import business, Star relocated its facilities to a smaller space, downsized its staff significantly and disposed of a lot of documentation it had generated while in the distribution business. Ms. Valenti cannot determine from Star's existing records the amount of its sales to Liquor Depot during 1994, 1995 and 1996. She forwarded her letter of August 28, 1997 based upon additional documentation supplied to her by a representative of Liquor Depot.

45. In August 1997, Mr. Aceto went to Star and spoke with Ms. Valenti. At that time, he showed her the actual purchase invoices for Liquor Depot's purchases from Star and canceled

checks for its payments to Star. The purchase invoices and canceled checks that he showed Ms. Valenti are not part of the record.

46. Mr. Aceto admitted that there is no way to know whether Liquor Depot actually had all the purchase invoices or whether some of the invoices had been misplaced, lost or intentionally removed. Mr. Aceto also admitted that the only way to verify the purchase amounts was to confirm such amounts with Liquor Depot's suppliers.

47. For the hearing, petitioners subpoenaed Ms. Valenti, the Star employee responsible for writing the August 28, 1997 letter to the Division (*see*, Finding of Fact "22"). However, Star refused to comply with the subpoena.

48. The Division's Research and Discovery Bureau located in Albany, New York collected sales information from various wholesale liquor suppliers during 1995. The supplier information provided to the Research and Discovery Bureau was submitted via magnetic tape. The Research and Discovery Bureau collected sales information from ten suppliers, including Star that reported sales to Liquor Depot during 1995. The total amount of Liquor Depot's 1995 purchases that Star separately confirmed to the Research and Discovery Bureau via magnetic tape was \$65,627.00. The total amount of Liquor Depot's 1995 purchases that Star confirmed to the auditors pursuant to the handwritten third-party confirmations was \$65,623.00.

49. The record includes a third-party verification reconciliation for 1995 prepared by the auditor. In this document, the auditor compared the 1995 supplier sales amounts confirmed to the auditor by six wholesale liquor suppliers, including Star, with the 1995 supplier sales amounts provided by those six suppliers to the Research and Discovery Bureau via magnetic tape, noted the difference, if any, and computed the percentage variation.

None of the differences between (i) the 1995 supplier sales amounts confirmed to the auditor by the wholesale liquor suppliers via the written third-party confirmations and (ii) the 1995 supplier sales amounts provided to the Research and Discovery Bureau via magnetic tape, were greater than 1%. In the case of Star, the difference was 00.006%.

50. The Audit Division has obtained sales information from Star for other taxpayers and, even in contested cases, the Audit Division has not had problems with the information it has obtained from Star.

51. During the audit period, Liquor Depot's customers included tax exempt organizations. Initially, Mr. Aceto maintained a looseleaf binder wherein he secured a separate exempt organization certificate for each organization to whose representative Liquor Depot sold alcoholic products. As sales were made, Mr. Aceto recorded them on looseleaf sheets of paper secured in the looseleaf binder, reflecting the total amount purchased by each organization.

52. At some point during the audit period, Mr. Aceto began to maintain separate sales order books for each alleged nontaxable organization, which contained separate sales invoices, on a daily basis, for sales of specific items sold to each organization. Each sales invoice contained information about every product sold including, among other things, its name, the quantity sold, Liquor Depot's purchase price and the price at which Liquor Depot sold it to the organization. Mr. Aceto never showed the sales order books containing the sales invoices to the auditor during the audit. Mr. Aceto threw out all of the sales order books containing the sales invoices for the period at issue after the audit was completed. The sales order books thrown out took up only approximately five to ten boxes to store.

53. The looseleaf binder containing information concerning the alleged exempt sales is part of the record. The looseleaf binder contains 24 exemption certificates. As was noted by the

auditor when he reviewed the contents of the looseleaf binder, the majority of the certificates bear dates prior to the opening of Liquor Depot (*see*, Finding of Fact “19”) . Liquor Depot’s name and address appear in the vendor box of only one exemption certificate, that of Swiss Benevolent Society. One exemption certificate has no information on it other than the organization’s exempt organization certificate number. Looseleaf sheets of lined paper are associated with each exemption certificate. The name of the organization, the exempt organization certificate number, dates and dollar amounts are handwritten in pencil on the looseleaf sheets of paper. Transactions through December 31, 1994 are listed on the looseleaf sheets of paper.

54. Petitioners submitted into evidence a copy of one check representing the proceeds from one of Liquor Depot’s sales to a tax exempt organization, the Swiss Benevolent Society. The check, dated November 11, 1992, in the amount of \$7,505.00 represents payment for a purchase made at Liquor Depot by the Swiss Benevolent Society. The record includes a properly completed tax exempt certificate for that organization, bearing a date of November 11, 1992. The looseleaf sheet of paper pertaining to Liquor Depot’s \$7,505.00 sale to the Swiss Benevolent Society lists the date of the sale as November 5, 1992. A detailed sales invoice for Liquor Depot’s sale to the Swiss Benevolent Society is not part of the record. As noted above, the confirmation request sent by the auditor to the Swiss Benevolent Society was returned by the USPS as undeliverable.

55. Petitioners submitted into evidence summary sales ledger sheets which purport to substantiate \$1,087,404.00 in sales made by Liquor Depot to exempt organizations during the period December 1, 1991 through February 29, 1996. For the initial part of the audit period, Mr. Aceto listed only a daily total of all nontaxable sales on the summary sales ledger sheets, which

he purportedly tallied from the sales that he listed on the separate looseleaf sheets of paper for each alleged exempt organization. For the period January 1995 through February 1996, the summary sales ledgers list, on a daily basis, the amount of each sale made to an alleged exempt organization as well as the total of all such sales and also the total for the particular month. For the period January 1995 through February 1996, the summary sales ledger sheets do not provide any information about the identity of the alleged exempt organization, the exact products sold or the price at which they were sold.

A review of the November 1992 summary sales ledger sheet indicates that sales were made to tax exempt organizations on 21 days including November 5, 1992, the date of the sale to the Swiss Benevolent Society. The daily total listed on the summary sales ledger sheet for November 5, 1992 is \$456.00, not \$7,505.00 - - the amount of Liquor Depot's sale to the Swiss Benevolent Society. No sales were listed for November 11, 1992.

56. Along with its brief, the Division submitted 83 proposed findings of fact. In accordance with State Administrative Procedure Act § 307(1), the Division's proposed findings of fact have been generally accepted with the following exceptions:

(a) Proposed findings of fact 6, 7, 21, 28, 32, 40, 54 and 65 were not adopted because they concerned evidentiary rulings and were deemed more appropriate to a discussion concerning the weight to be given to certain evidence rather than to the findings of fact.

(b) Proposed finding of fact 53 has been modified to more accurately reflect the record.

(c) Proposed findings of fact 71, 80, and 82 are repetitive of other proposed findings of fact.

(d) Proposed finding of fact 83 is not a proposed finding of fact, it is an explanation of a method used in findings of fact.

SUMMARY OF THE PARTIES' POSITIONS

57. Petitioners contend that the Division made numerous glaring errors in its determination that additional sales taxes are due for the period in issue. First, they assert that Liquor Depot maintained adequate books and records reflecting its total sales and its taxable and nontaxable sales. Petitioners argue that Liquor Depot's records clearly substantiate the substantial volume of sales, \$1,087,404.00, that it made to tax exempt organizations during the period in issue. They assert that the Division did not undertake an appropriate audit to verify that Liquor Depot's tax exempt sales were not, in fact, tax exempt. In the alternative, if petitioners did not meet their burden with respect to proving nontaxable sales, they contend that the Division erred in applying a 25% markup to the claimed tax exempt sales in lieu of the actual markup ranging from between 3% and 9% during the audit period. Second, with respect to the Division's determination that Liquor Depot had made \$566,598.00 in purchases from Star, petitioners argue that the evidence clearly establishes that Liquor Depot's purchases from Star were minimal, totaling only \$6,391.03 for the entire audit period and that the Division erred in attributing those additional purchases to Liquor Depot. Third, with respect to the Division's markup analysis of Liquor Depot's purchases, petitioners argue that Liquor Depot's markups on wine and liquor were significantly lower during the earlier quarters of the audit period than the markups during the later quarters and that the Division failed to take that into consideration in its determination of the 25% markup on sales. Further, petitioners claim that the markup determined by the Division fails to give a proper allowance for coupon sales, discount sales or losses for breakage and pilferage. Lastly, petitioners contend that the penalties should be abated. They claim that Mr. Aceto, an individual unsophisticated in financial or business practices, with no formal accounting education or experience, who was ignorant of even the most rudimentary

accounting and tax practices, fully relied on his long-term accountant to maintain Liquor Depot's books and records and report its tax.

58. The Division asserts that its determination of additional sales tax due is proper. It argues that since petitioners failed to maintain proper and adequate books and records, the Division was justified in estimating Liquor Depot's sales tax liability using external sources of information. The Division contends that its use of questionnaires sent to Liquor Depot's customers is an appropriate and reasonable method for determining whether certain sales are exempt from taxation. The Division admits that the assessment should be adjusted because of evidence submitted by petitioners at the hearing concerning the \$7,505.00 purchase made by the Swiss Benevolent Society, a tax exempt organization. However, the Division argues that petitioners have failed to substantiate any other purchases by tax exempt organizations. The Division claims that the use of third-party information obtained from Liquor Depot's wholesale liquor suppliers is an appropriate and reasonable method for calculating actual sales. It argues that petitioners have failed to prove by clear and convincing evidence that the information originally supplied by Star to the Division is incorrect. With respect to the markup percentage determined by the Division, it was calculated based on a limited markup test of Liquor Depot's shelf prices as well as discussions with Mr. Aceto. As for petitioners' assertion that lower markup percentages were used for sales made to what petitioners claimed were tax exempt entities, the Division points out that Liquor Depot's source records were destroyed and it is impossible to verify their assertion. As for the penalties, the Division argues that petitioners have failed to show that the delinquency was due to reasonable cause or the absence of willful neglect. The Division claims that the evidence clearly establishes that Mr. Aceto, the sole

owner, was a business man with considerable experience in the retail liquor industry and that petitioners' reliance on their accountant was unjustified.

59. In their reply brief, petitioners concede that during the initial audit Mr. Aceto did not provide the auditors with records because he did not then maintain the same. They also claim that "before the examination concluded, and certainly during the hearing, [Mr. Aceto] submitted appropriate documentation which would have enabled the auditors to accurately reflect the appropriate markup and determine the correct amount of taxable and nontaxable sales" (Petitioners' reply brief, p. 3). As for the purchase verification undertaken by the Division, petitioners maintain that Mr. Aceto's analysis with respect to most of Liquor Depot's purchases substantially agrees with the Division's analysis. Petitioners take exception to the Division's determination that Liquor Depot made \$566,598.00 in purchases from Star. They argue that if Star's analysis is incorrect from the beginning, it is incorrect overall, notwithstanding the information given to the Research and Discovery Bureau or to the auditor. Petitioners assert that, even if Mr. Aceto's determination of over \$1,000,000.00 in tax exempt sales is incorrect, based on the evidence submitted during the audit and at the hearing, the Division should have used a markup of 3% to 9% for those additional sales to determine petitioners' tax liabilities. Further, petitioners contend that contrary to the Division's assertion, Mr. Aceto did in fact advise the auditors of a significantly reduced markup for sales of "hot items" or discounted coupon sales. Lastly, petitioners assert that the record clearly establishes that, because he was truly unsophisticated in financial and business practices, Mr. Aceto had no way of knowing that the tax treatment undertaken by his long-term accountant was improper and did not accurately reflect the proper tax treatment of the sales made by Liquor Depot.

CONCLUSIONS OF LAW

A. It is well established that every person required to collect tax must maintain and make available for audit upon request records sufficient to verify all transactions in a manner suitable to determine the correct amount of tax due (Tax Law § 1135[a]; 20 NYCRR 533.2[a]). Failure to maintain and make available such records, or the maintenance of inadequate records, will result in the Division of Taxation's estimating tax due (Tax Law § 1138[a]; *see, Matter of Ristorante Puglia, Ltd. v. Chu*, 102 AD2d 348, 478 NYS2d 91, 93; *Matter of Surface Line Operators Fraternal Org. v. Tully*, 85 AD2d 858, 446 NYS2d 451, 452). To determine the adequacy of a taxpayer's records, the Division of Taxation must first request and thoroughly examine the taxpayer's books and records for the entire period of the proposed assessment. The purpose of such an examination is to determine whether the records are so insufficient as to make it virtually impossible to verify taxable sales receipts and conduct a complete audit (*Matter of Adamides v. Chu*, 134 AD2d 776, 521 NYS2d 826, 828, *lv denied* 71 NY2d 806, 539 NYS2d 109; *Matter of King Crab Rest. v. State Tax Commn.*, 134 AD2d 51, 522 NYS2d 978).

B. The original appointment letter and the subsequent appointment letter, which extended the audit period, sent by the Division to petitioners constituted an adequate request for books and records and, taken together, cover the entire audit period in issue. This was followed by several other written requests for records and telephone conversations discussing the providing of records and meetings wherein records were requested. The records provided by petitioners consisted of federal income tax returns for the years 1991, 1992, 1993 and 1994, bank statements for December 1991 through December 1994, the check disbursements journal and canceled checks, including a number of checks showing purchases made from some liquor suppliers, for the period December 1993 through November 1994. Late in the audit, Mr. Aceto produced a

looseleaf binder and sales summary ledger sheets containing information that he claimed supported nontaxable sales of approximately \$1,047,907.50 to exempt organizations for the period December 1, 1991 through December 31, 1995. Given the magnitude of the claimed sales to exempt organizations, the auditor sent written confirmation requests to the organizations to which Liquor Depot claimed it made nontaxable sales. The auditor noted that the responses from the organizations confirmed a total of only \$776.16 in nontaxable sales for the audit period. Petitioners provided no cash register tapes, sales journal, sales invoices, purchase invoices or receipts reflecting cash payments to wholesale liquor suppliers for its purchases. The audit report and the auditor's testimony reflect that the records provided to the Division were reviewed and determined to be inadequate. On the basis of the foregoing, it is clear that Liquor Depot's records were inadequate to conduct a complete audit. Therefore, it was acceptable for the Division to calculate petitioners' tax liability based on external indices, which in this case was a third-party purchase confirmation markup audit.

C. Petitioners assert that the Division incorrectly determined that Liquor Depot's purchases from Star totaled \$566,598.00 during the audit period. They claim that the evidence overwhelmingly establishes that Liquor Depot's purchases were minimal, totaling only \$6,391.03 during the audit period. They aver that the Division, during the audit and at the hearing, received proof showing that the purchase amounts originally verified by Star were incorrectly prepared using information pertaining to another account and that it failed to pursue this issue. Petitioners contend that Mr. Aceto's testimony, and the August 28, 1997 letter from Star's controller, Ms. Valenti, along with his attempts to secure Ms. Valenti's testimony, which were ignored by Star, support his position that the Division's calculation of Liquor Depot's purchases from Star is wrong.

I do not find Ms. Valenti's August 28, 1997 letter and Mr. Aceto's testimony to be sufficient to prove that the Division's calculation of Liquor Depot's purchases from Star is incorrect. I find Ms. Valenti's August 28, 1997 letter to be deficient in many ways. First, Ms. Valenti did not prepare either of the written confirmations sent to the auditor. Nor was she responsible for supervising the Star employees assigned to prepare either of those purchase confirmations. Second, she based her letter on documentary evidence supplied by Mr. Aceto, not a review of Star's records. Third, while she states that the originally confirmed purchase figures are wrong, she fails to either identify the extent of the error or the correct figures. If the purchase invoices presented to Ms. Valenti by Mr. Aceto totaled only \$6,391.03 as Mr. Aceto claimed at the hearing, I find it incredible that, in her letter, Ms. Valenti made no comment about the huge difference in the figures contained in the purchase confirmations sent by Star and those set forth in Liquor Depot's purchase invoices. The record includes the purchase summary sheets prepared by Mr. Aceto which purport to be a summary of all original purchase invoices substantiating Liquor Depot's purchases from five of its suppliers, including Star, for the audit period. Mr. Aceto testified that he used the actual purchase invoices to prepare those purchase summary sheets. However, it is impossible to verify the accuracy of the figures pertaining to Liquor Depot's purchases from the supplier Star set forth on the purchase summary sheets because petitioners failed to introduce the source documents, i.e., the purchase invoices that represented Liquor Depot's purchases from the supplier Star, into the record. Petitioners have failed to show by clear and convincing evidence that the assessment was erroneous on this basis (*Matter of Meskouris Bros. v. Chu, supra*).

D. Petitioners argue that the Division did not undertake an appropriate audit to verify that Liquor Depot's tax exempt sales were not, in fact, tax exempt. They assert that the auditor did

nothing more than send out written confirmation requests and, when they were not answered, or when shown to be answered incorrectly, the auditor did not follow up. Petitioners further claim that Liquor Depot's records clearly substantiate the substantial volume of sales, \$1,087,404.00, that it made to tax exempt organizations during the audit period. Petitioners maintain that the records showed the name of each organization, the date of each sale and the total amount of each sale. They contend that Liquor Depot's record keeping left the means whereby its sales reported as exempt could be tied to or compared with its exemption certificates.

Petitioners argument that the Division did not undertake an appropriate audit of Liquor Depot's alleged exempt sales is rejected. At the last field audit appointment, Mr. Aceto presented the auditor with a looseleaf binder containing information and summary ledger sheets that he claimed supported nontaxable sales to exempt organizations. That looseleaf binder contained 24 exempt organization certificates and looseleaf sheets of paper. A review of the exemption certificates by the auditor revealed that the vendor portion was not filled in on the majority of the exemption certificates and most of the dates written on the certificates were prior to the date on which Liquor Depot began business. One exemption certificate had no information on it other than the organization's exempt organization certificate number. Despite the fact that the vast majority of the exemption certificates were not properly completed, the auditor decided to confirm the amount of Liquor Depot's claimed exempt sales directly with each of the 23 organizations listed on the exemption certificates. However, only twelve tax exempt organizations responded to the Division's written requests. Only two of the twelve tax exempt organizations confirmed purchases from Liquor Depot during the audit period. The auditor was able to verify only \$776.16 in nontaxable sales, and these verified exempt sales were deducted in arriving at audited taxable sales.

Petitioners contend that Liquor Depot's records substantiate \$1,807,404.00 in sales made by it to exempt organizations during the audit period. To demonstrate that the sales at issue are nontaxable, petitioners must show that the purchaser is an exempt organization and present adequate documentation confirming the existence and accuracy of the alleged exempt sale (*Matter of On the Rox Liqs., Ltd. v. State Tax Commn.*, 124 AD2d 402, 507 NYS2d 503, 505, *lv denied* 69 NY2d 603, 512 NYS2d 1026). A properly completed exemption certificate containing the date prepared; name and address of the purchaser; name and address of the vendor; the exempt organization number as shown on the exempt organization certificate and the signature of the purchaser's authorized representative satisfies petitioners' burden of showing that the purchaser is an exempt organization (*see*, 20 NYCRR 532.4[b][2][ii]). At the hearing, petitioners submitted the looseleaf binder containing 24 exemption certificates and associated looseleaf sheets of paper, and summary sales ledger sheets which purport to substantiate their nontaxable sales into evidence. A review of the 24 exemption certificates reveals that only one exemption certificate, listing the Swiss Benevolent Society as purchaser, is properly completed. During the audit, the auditor was unable to confirm any purchases by the Swiss Benevolent Society because the confirmation request was returned by the USPS as undeliverable. However, the auditor did confirm purchases by two organizations. Even though the exemption certificates pertaining to those two sales were not properly completed, the auditor treated those sales as nontaxable. At the hearing, petitioners submitted a copy of a canceled check in the amount of \$7,505.00. The Swiss Benevolent Society is the maker of this check and Liquor Depot is the payee. The Division concedes that taxable sales should be reduced by \$7,505.00 and the assessment adjusted accordingly. Petitioners have failed to prove that any additional sales were made to exempt organizations during the audit period.

E. Petitioners claim that the Division erred in applying the overall markup of 25% to the disallowed nontaxable sales. They argue that the actual markup for those sales ranged from 3% to 9% during the audit period. In support of their argument, petitioners offered the testimony of Mr. Aceto, the looseleaf binder containing exemption certificates and associated sheets of looseleaf paper, summary sales ledger sheets which list the sales made by Liquor Depot to alleged exempt organizations during the period December 1, 1991 through February 29, 1996 and a representative example⁴ of the sales order book, containing separate sales invoices, maintained for each alleged exempt organization. Mr. Aceto testified that initially his markup on sales to tax exempt organizations was 3% and gradually he raised it. He further testified that the markup was 9% for most of the audit period. In order to verify Mr. Aceto's testimony it is necessary to perform a markup test. In order to calculate the markup percentage, it is necessary to have sales invoices that specifically list the identity, quantity, purchase price and selling price of the items sold. However, it is impossible to perform such a test using the documents in the record. The looseleaf sheets of paper associated with each exemption certificate reflect only the total amount of each alleged purchase. The summary sales ledger sheets list a daily total of all alleged sales made to alleged exempt organizations. Although Mr. Aceto maintained separate sales invoices for each alleged exempt organization during the audit period, he failed to show those invoices to the auditor. He threw those invoices away after the audit was completed. The representative example of the sales invoices cannot be used either. The invoices memorialize sales that took place after the audit period ended. Petitioners have failed to show by clear and convincing evidence that the assessment was erroneous on this basis (*Matter of Meskouris Bros. v. Chu, supra*).

⁴ The representative example sales order book is for a period after the audit period ended.

F. Petitioners claim that Liquor Depot's markups on wine and liquor were significantly lower during the earlier quarters of the audit period than the markups during the later quarters and that the Division failed to take that into consideration in its determination of the 25% markup on sales. The only evidence proffered in support of this claim is Mr. Aceto's testimony which consisted of vague statements that his markups on wine and liquor were lower in the earlier quarters of the audit period. Mr. Aceto did not specifically state what his markups on wine and liquor were during the early quarters of the audit period. Petitioners have failed to show by clear and convincing evidence that the assessment was erroneous on this basis (*Matter of Meskouris Bros. v. Chu, supra*).

G. Petitioners claim that the markup determined by the Division fails to give a proper allowance for coupon sales and discount sales. Based on his discussions with Mr. Aceto, the auditor gave a 3% allowance to account for special sales and any other significant discounts offered by Liquor Depot to its customers. Petitioners have failed to identify what would be an appropriate allowance for coupon sales and discount sales. The only evidence of the proper allowance was Mr. Aceto's vague testimony that he did not know what percentage of his sales were attributable to coupon sales and discount sales. Petitioners have failed to show by clear and convincing evidence that the assessment was erroneous on this basis (*Matter of Meskouris Bros. v. Chu, supra*).

H. Petitioners argue that the Division did not give a proper allowance for pilferage and breakage. The auditor allowed a 1½% reduction in purchases for pilferage and breakage based upon the Audit Division's experience in the liquor retail industry and because the adjustment is required by Field Audit Management. Petitioners have failed to identify what would be an appropriate allowance. The only evidence of the proper allowance was Mr. Aceto's vague

testimony that he had no idea what was stolen from inventory and that there was significant breakage. Given petitioners' failure to prove the amount of pilferage and breakage loss experienced at Liquor Depot, the Division's 1½% allowance for pilferage and breakage is adequate (*see, Matter of Shop Rite Wines & Liquors, Inc.*, Tax Appeals Tribunal, February 22, 1991).

I. Section 1145(a)(1)(i) authorizes the imposition of penalty for the failure to file a return or to pay or pay over the sales and use taxes due within the time required. Section 1145(a)(1)(vi) of the Tax Law authorizes the imposition of penalty upon a taxpayer for its omission from the total amount of sales and use taxes required to be shown on a return an amount which is in excess of 25% of the amount of such taxes required to be shown on the return. The commissioner may abate all penalty, pursuant to section 1145(a)(1)(iii) and (vi), when it is determined that such omission was due to reasonable cause and not due to willful neglect. Reasonable cause includes any cause for delinquency which would appear to a person of ordinary prudence and intelligence as reasonable cause for the delay in filing a sales tax return and paying the tax imposed under Articles 28 and 29 of the Tax Law (20 NYCRR former 536.5[c][5]).

Petitioners contend that penalties should be abated because Mr. Aceto, an individual unsophisticated in financial or business practices, with no formal accounting education or experience, who was ignorant of even the most rudimentary accounting and tax practices, fully relied on his long-term accountant to maintain Liquor Depot's books and records and report its tax. They further argue that because he was truly unsophisticated in financial and business practices, Mr. Aceto had no way of knowing that the tax treatment undertaken by his long-term

accountant was improper and did not accurately reflect the proper tax treatment of the sales made by Liquor Depot.

I find that the Division properly assessed penalties in this matter. First, penalties are appropriate in this case because there is a substantial discrepancy between the sales tax reported on the returns and the sales tax found to be due on audit (*see, Matter of S.H.B. Super Markets, Inc. v. Chu*, 135 AD2d 1048, 522 NYS2d 985). Second, the record clearly establishes that Mr. Aceto is a businessman with considerable experience in the retail liquor industry. Petitioners' claims of Mr. Aceto's lack of sophistication in financial and business practices belies the facts in the record. Mr. Aceto actively ran Liquor Depot on a daily basis. He negotiated payment terms with the liquor suppliers and dealt with their credit managers. Given Mr. Aceto's knowledge that, within months of opening, Liquor Depot began paying many of its suppliers in cash, his reliance on his accountant's preparation of the sales tax returns based on deposits listed on the bank statements was not reasonable.

J. The petition of Liquor Depot is granted to the extent of Conclusion of Law "D" and the Division is directed to modify the Notice of Determination, dated May 26, 1998, accordingly; except as so granted, the petition is otherwise denied and the Notice of Determination is sustained.

The petition of Frank Aceto is granted to the extent of Conclusion of Law "D" and the Division is directed to modify the Notice of Determination, dated May 26, 1998, accordingly, except as so granted, the petition is otherwise denied and the Notice of Determination is sustained.

DATED: Troy, New York
March 7, 2002

/s/ Winifred M. Maloney
ADMINISTRATIVE LAW JUDGE